

Office of Chief Counsel  
Internal Revenue Service

**memorandum**

CC:LM:MCT:PHI:TL-N-5295-00  
LSBednarz

date:

to: **Jack Cohen, Team Manager**  
**LMSB: Manufacturing, Construction & Transportation**  
**Group 1343, King of Prussia, PA    Attn: Russell G. Mayall**  
**Team Coordinator**

from: **James C. Fee, Jr.**  
**Associate Area Counsel (LMSB)**

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subject: [REDACTED] - ITC Claim  
**MITIGATION - AUTHORITY TO ASSERT DEFICIENCIES IN**  
**BARRED YEARS**

THIS WRITING MAY CONTAIN PRIVILEGED INFORMATION. ANY UNAUTHORIZED DISCLOSURE OF THIS WRITING MAY HAVE AN ADVERSE EFFECT ON PRIVILEGES, SUCH AS THE ATTORNEY-CLIENT PRIVILEGE. IF DISCLOSURE BECOMES NECESSARY, PLEASE CONTACT THIS OFFICE FOR OUR VIEWS.

This memorandum is in response to your request for legal advice concerning the assertion of deficiencies against [REDACTED] in years barred by the statute of limitations. This memorandum should not be cited as precedent.

You have presented us with the following factual situation:

The taxpayer, [REDACTED] has filed amended income tax returns for the years [REDACTED] through [REDACTED], claiming additional investment tax credit under Sections 203 and 204 of the TRA of [REDACTED]. For each of the years [REDACTED] through [REDACTED], the taxpayer was in an excess tax credit carryforward situation, having used the allowable general business credit limitation for each year. Thus, any additional credits would be carried forward, and would be fully utilized in [REDACTED]

The Tax reform Act of 1986 requires a taxpayer to reduce the basis of assets, for which ITC is claimed, by 100% of the amount of the eligible ITC. The reduction in basis will result in a reduction in depreciation for the source year of the credit and all subsequent years for the life

of the asset. The reduced depreciation will result in additional taxable income and an increase in the gross amount of tax. The additional gross tax increase will be offset in part by the additional ITC allowable, up to the general business credit limitation amount. However, the general business credit limitation does not offset in full the increase in tax from the disallowance of depreciation, this will result in a deficiency in the source years, [REDACTED] through [REDACTED].

The statute of limitations had expired for the years [REDACTED] through [REDACTED] prior to the time the claims for refund were filed. The statute of limitations for the years [REDACTED] through [REDACTED] is open under a restricted Form 872, which provides that the statute remains open for ITC and any adjustments (including depreciation) resulting from the taxpayer's claim for additional ITC. The statute of limitations for the years [REDACTED] through [REDACTED] is open under a Form 872 (unrestricted).

The taxpayer has been examined for the years [REDACTED] through [REDACTED]. The years [REDACTED] through [REDACTED] are currently in Appeals. The years [REDACTED] through [REDACTED] are currently under examination.

You have asked for legal advice on the following questions:

(1) Can the deficiencies which will arise in the years [REDACTED] through [REDACTED] if additional ITC is allowed, be assessed for those barred years under Sections 1311 through 1314?

(2) If not, do we adjust depreciation in each year [REDACTED] through [REDACTED] creating barred deficiencies or do we adjust depreciation beginning in the first open year ([REDACTED])?

As you are aware, it is the position of the Service that the failure to claim investment tax credit on Section 38 property placed in service in a year for which the statute of limitations has expired, does not prevent any unused credit from being carried over to an open year under Section 46(b). Rev. Rul. 82-49, 1982-1 C.B. 5. This position has previously been applied by the Courts. In Mennuto v. Commissioner, 56 T.C. 910 (1971), acq. 1973-2 C.B. 2, the Court held that the service could recompute a investment tax credit in a barred year, to determine the proper amount of investment tax credit carryover to an open year. See also State Farming Co. v. Commissioner, 40 T.C. 774 (1963) and Rev. Rul. 69-543, 1969-2 C.B. 1. A similar rule applies for net operating loss carry overs. Rev. Rul. 81-88, 1981-1 C.B. 585. Thus, ITC can be carried forward to open years even though the statute of limitations for the source years has expired.

You have asked whether a deficiency can be asserted in the source years where the statute of limitations has expired (██████ through ██████) under the mitigation provisions of Sections 1311 through 1314. It is our position that no deficiency can be asserted in the barred years.

Sections 1311 through 1314 are relief provisions which essentially provide that where a determination for one tax year is made with respect to an item which was erroneously treated for a prior year, for which the statute of limitations has expired, the prior year can be reopened to correct the error and prevent a party from incurring a double tax advantage or disadvantage. Under these mitigation provisions, Section 1311 (b)(1)(A) requires that the party against whom Section 1311 is applied (here, the IRS) must have taken an inconsistent position.

In the present case, no inconsistent position is taken. In this case, the taxpayer is merely claiming additional ITC which it failed to claim in the barred source years. As a result, depreciation, alternative minimum tax, and other amounts on the original returns for the barred source years, may need to be adjusted as a result of the unclaimed ITC. These adjustments, however, do not constitute an inconsistent position by the IRS (or the taxpayer). The mitigation provisions, therefore, are not applicable.

The standard treatment in such situations has been long-established by the IRS and the courts. Although the deficiencies for barred years cannot be asserted, the amount of the carry over can be properly computed and asserted in open years. In Hill v. Commissioner, 95 T.C. 437 (1990), the issue was whether the IRS could recompute the tax for a prior barred year and, because of the recomputation, decrease the amount of unused investment credit to be carried over to a subsequent open year. The Court found that the IRS was entitled to make such a computation. The Court stated that, "The critical element is that the deficiency being determined is for a year on which the period of limitations has not run... Indeed, in that open year... a taxpayer may be forced to contest respondent's adjustments for a year long past in a dispute regarding the proper amount of a deficiency determined for the open year.", *Id.* at 444. In support of its decision, the Tax Court cited Mennuto v. Commissioner, 56 T.C. 910 (1971), *acq.* 1973-2 C.B. 2, Rev. Rul. 69-543, 1969-2 C.B. 1 and various cases dealing with net operating loss carry backs and carry forwards. In discussing the basis for its reasoning in such situations, the Court in The State Farming Company, Inc. v. Commissioner, 40 T.C. 774, 781 (1963), explained: "We do not believe that the purpose of the carryover provisions will allow us to place petitioners in a better position because the relevant events were spread over a period of time rather than in a single year."

In answer to your second question, basis should be properly reduced for the credit amount and the depreciation claimed for the barred years, even though no deficiency can be asserted. For the open years (up to and including ██████ where the carry forward is depleted), depreciation should be properly computed on the basis as adjusted. An adjustment can be

made in [REDACTED], the first open year under the restricted consent, as well as [REDACTED] through [REDACTED]. If a deficiency arises in [REDACTED] or the following open years, as a result of the depreciation adjustment or adjustments relating to the increase in investment tax credit, such deficiency can be asserted against the taxpayer.

A copy of this memorandum is being forwarded to our national office for post-review pursuant to our manual Section (35)3(19)4. If our national office makes any significant changes to our advice, we will notify you within ten business days.

Please feel free to contact Attorney Linda S. Bednarz at (215) 597-3442 if you have any further questions regarding this matter.

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JAMES C. FEE, JR.  
Associate Area Counsel (LMSB)